

# DP IB Business Management: HL



Your notes

## 3.3 Costs & Revenues

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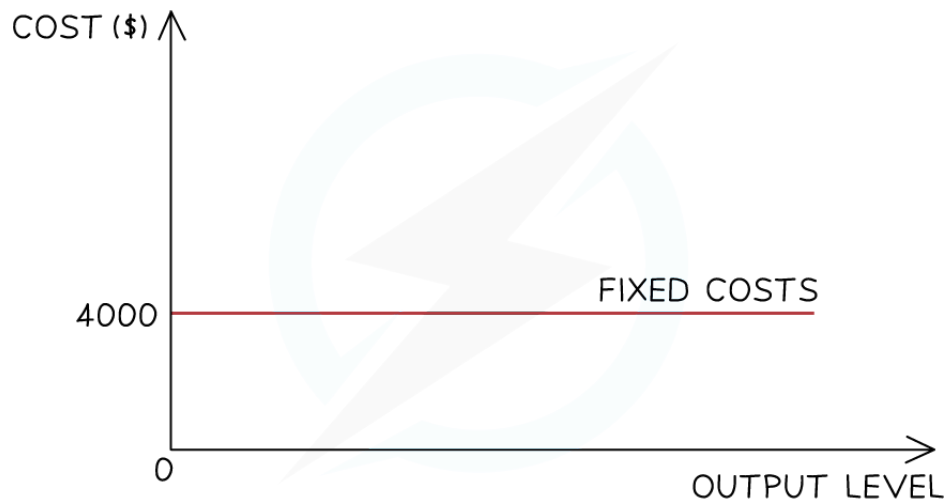
## Types of Costs

# An Introduction to Costs

- In preparing goods and services for sale, businesses **incur a range of costs**
  - Some examples of these these costs include **purchasing raw materials**, paying staff salaries and wages, and **paying utility bills** such as electricity
- These costs can be broken into different categories
  - **Fixed costs (FC)** are costs that do not change as the level of output changes
    - These have to be paid whether the output is zero or 5000
  - **Variable costs (VC)** are costs that vary directly with the output
    - These increase as output increases & vice versa
  - **Total costs (TC)** are the sum of the fixed + variable costs

## Comparison of the Types of Cost

### Fixed costs (FC)



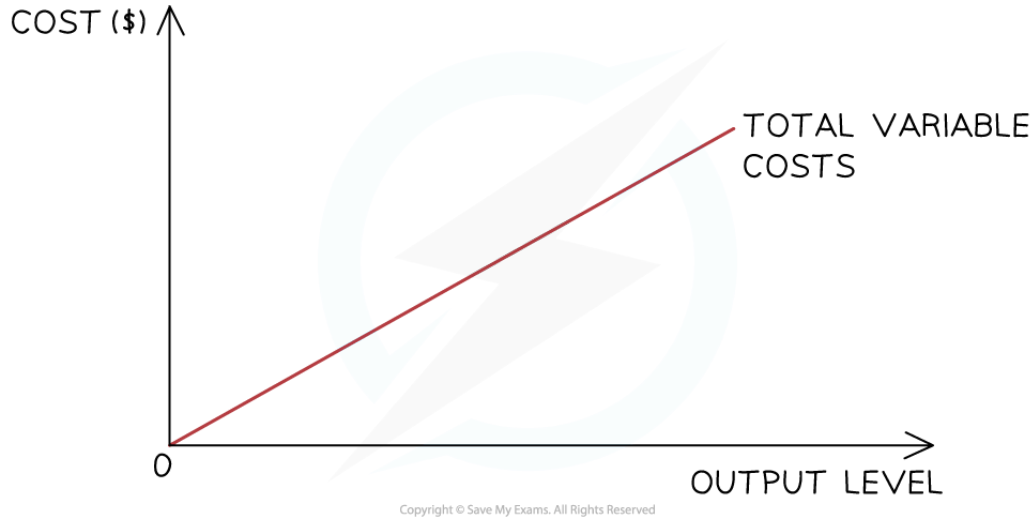
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- The firm has to pay its **fixed costs** which do not change, irrespective if the output is 0 or 100,000 units
- The fixed costs for this firm are \$4,000



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## Variable costs (VC)

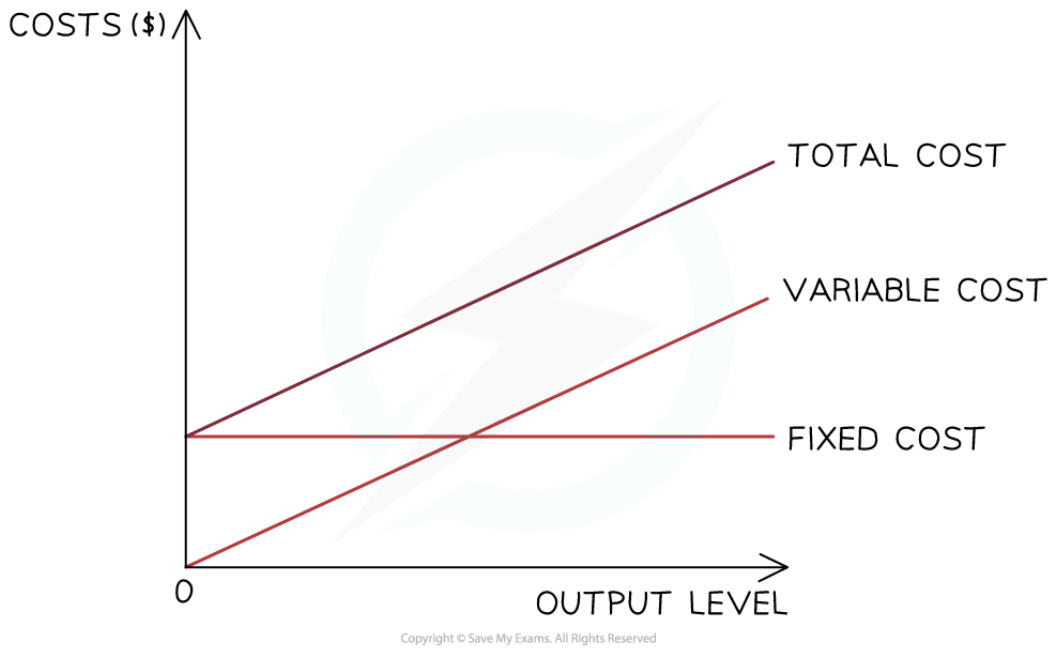


- The variable costs initially **rise proportionally with output**, as shown in the diagram
- At some point, the firm will benefit from a **purchasing economy of scale** and the rise will no longer be proportional

## Total costs (TC)



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- The **total cost** is the sum of the variable and fixed costs
- The total costs **cannot be 0** as all firms have some level of fixed costs

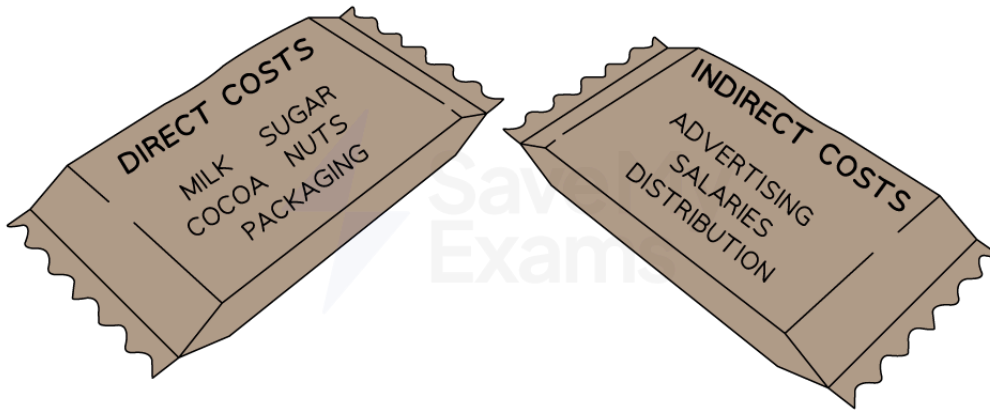
## Direct & Indirect Costs

- Direct costs are related to the production of a particular product and **vary directly with output**
  - Examples include raw materials, components and packaging
- Indirect costs cannot be allocated easily to the production of a particular product
  - They **relate to the business as a whole** and are often called **overheads**
  - Examples include administration costs, salaries and rental fees

## Diagram: direct and indirect Costs



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**Examples of direct and indirect costs for a chocolate manufacturer**



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## Sales Revenue

# Revenue & Revenue Streams

- Sales Revenue is the **value of the units** sold by a business over a period of time
  - E.g the revenue earned by Apple Music from sales of music downloads
  - Sales revenue is a **key business performance measure** and must be calculated to identify profit
  - Sales revenue is calculated using the formula

$$\text{Sales revenue} = \text{quantity sold} \times \text{selling price}$$

- Sales revenue **usually increases** as the **sales volume increases**
- When a firm sells one product it is easy to calculate the sales revenue
  - The more products a firm sells, the harder it is to calculate the sales revenue
  - **Computer systems** make it easier to track sales revenue when multiple products are sold by the business



### Worked Example

Fotherhill Organics Limited sold 39,264 packs of its specialist compost to mail-order customers in 2022. The price per pack was £8.75. In addition, it sold 4,275 tonnes to gardening businesses for £123.95 per tonne.

Calculate Fotherhill Organics sales revenue for 2022? [3 marks]

Answer:

**Step 1 – Calculate the sales revenue from sales to mail-order customers**

$$39,264 \times £8.75 = £343,560 \quad [1]$$

**Step 2 – Calculate the sales revenue from sales to gardening businesses**

$$4,280 \times £123.95 = £530,506 \quad [1]$$

**Step 3 – Add together the two sales revenue figures**

$$£343,560 + £530,506 = £874,066 \quad [1]$$

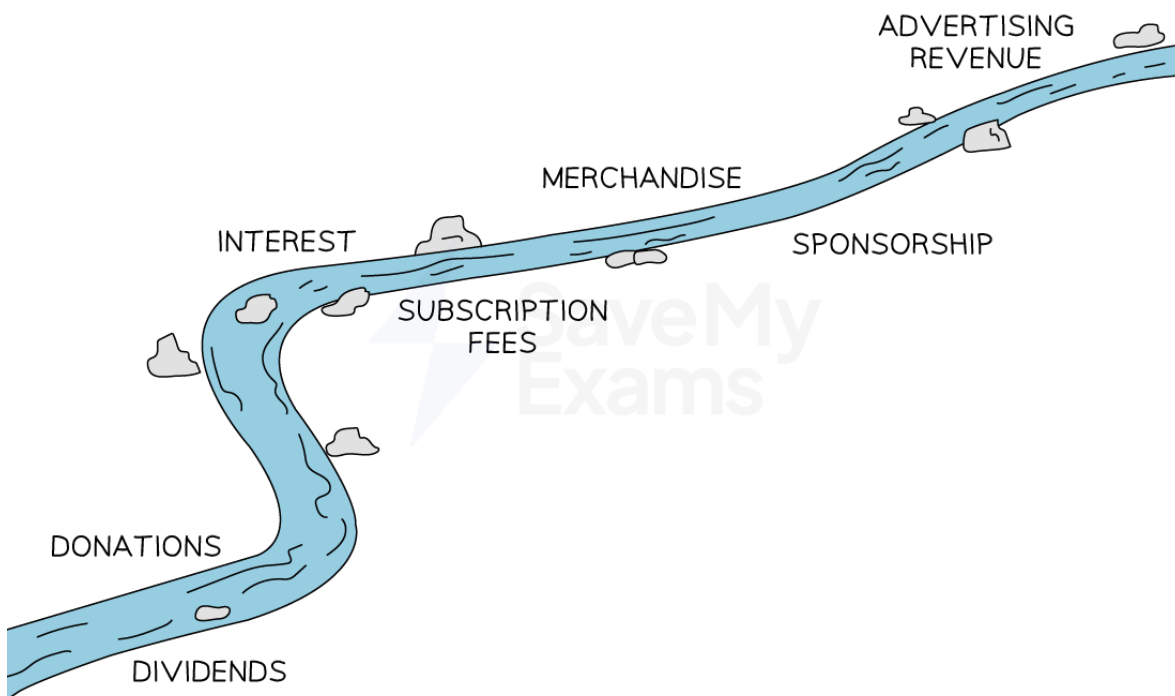


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## Revenue streams

- Revenue can be generated from sources other than sales
- These sources are called **revenue streams**

### Diagram: revenue streams



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*Some examples of revenue streams for businesses*

#### An Explanation of Revenue Streams

Revenue Stream	Explanation	Example
<b>Dividends</b>	<ul style="list-style-type: none"> <li>Businesses sometimes <b>purchase shares in other companies</b> and may be entitled to <b>dividends</b></li> </ul>	<ul style="list-style-type: none"> <li>The UK's leading supermarket Tesco received more than <b>£68m in dividends in 2023</b> from its investments in a range of property companies</li> </ul>



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	<ul style="list-style-type: none"> <li>For <b>holding companies</b>, dividends are the primary source of revenue</li> </ul>	
<b>Donations</b>	<ul style="list-style-type: none"> <li>An important source of revenue for not-for-profit organisations such as <b>charities</b></li> </ul>	<ul style="list-style-type: none"> <li>In 2022 Oxfam received <b>over £70m of revenue in the form of donations</b> and legacies</li> </ul>
<b>Interest</b>	<ul style="list-style-type: none"> <li>Many businesses hold substantial amounts of cash as <b>bank deposits which earn interest</b></li> </ul>	<ul style="list-style-type: none"> <li>Clothing retailer Zara's parent company Inditex earned £85m net interest revenue in 2022</li> </ul>
<b>Subscription fees</b>	<ul style="list-style-type: none"> <li>Some businesses earn the majority of their revenue from subscriptions that <b>allow users to access a product or service for a regular ongoing fee</b></li> <li>Subscriptions are also frequently offered alongside one-off purchases</li> </ul>	<ul style="list-style-type: none"> <li>In 2022 Netflix earned \$31.6 billion in subscription revenue in 2022, 40% of which was generated in North America, its largest market</li> </ul>
<b>Merchandise</b>	<ul style="list-style-type: none"> <li>Merchandise is a useful way to earn <b>additional revenue alongside core sales</b> of a product or service</li> </ul>	<ul style="list-style-type: none"> <li>As well as revenue earned from the <b>sale of broadcasting rights and ticket sales, official merchandise sales</b> during 2016's Rio de Janeiro Olympics reached \$15.5 million</li> </ul>
<b>Sponsorship</b>	<ul style="list-style-type: none"> <li>Some organisations attract sponsorship from businesses that are keen to <b>associate themselves with the brand</b></li> </ul>	<ul style="list-style-type: none"> <li>In 2022 FC Barcelona received more than \$215 million of <b>sponsorship revenue from 35 worldwide sponsors</b> including Nike, Coca Cola and Allianz Bank</li> </ul>
<b>Advertising Revenue</b>	<ul style="list-style-type: none"> <li>Online media businesses - in particular social media - generate the majority of their <b>revenue from advertising</b></li> </ul>	<ul style="list-style-type: none"> <li>In 2022 social media giant Twitter earned \$4.14 billion in advertising revenue</li> </ul>